

Lessors of tangible personal property under true leases in Illinois are deemed end users of the property to be leased. See 86 Ill. Adm. Code 130.220. (This is a GIL).

December 5, 2001

Dear Xxxxx:

This letter is in response to your letter received August 27, 2001. The nature of your letter and the information you have provided require that we respond with a General Information Letter, which is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120(b) and (c), which can be found on the Department's website at <http://www.revenue.state.il.us/legalinformation/regs/part1200>.

In your letter, you have stated and made inquiry as follows:

We are writing this letter to request a written opinion on a sales/use tax issue.

AAA is in the business of providing retail installment contracts for vehicles. One type of retail installment contract offered by AAA (which will be identified as balloon contract) is a contract not payable in installment of equal amounts. The last scheduled payment (the 'balloon payment') is substantially larger than each of the other scheduled payments. In this balloon contract the vehicle is owned and titled by the customer with payments for the vehicle made to AAA. At the end of the contract the customer has three options: (1) Pay the balloon payment on or before its due date (2) return the vehicle to AAA (3) at the time the balloon payment is due, refinance the amount remaining due under the contract.

Our question pertains to customers who choose not to purchase the vehicle and return the vehicle to AAA. Written in the balloon contract is the following:

'Return the vehicle to us and pay any late charges and other amounts due...a \$400 vehicle disposal fee, and Excess Wear and Tear Deduction and/or excess mileage deduction.'

The excess wear and tear deduction is defined as follows: The excess wear & tear deduction shall be the amount which it would cost AAA to put the vehicle in good working order and condition, whether or not we make the repairs.

The Base Mileage allowed (before the due date of the Balloon Payment) is shown on the face of the contract. The excess mileage deduction is defined as follows: if the

mileage on the vehicle at the end of the contract period is higher than shown on the balloon contract, the customer agrees to pay an excess mileage deduction at the rate of 15 cents per mile that exceeds the base mileage allowed.

We would like a letter ruling on the following:

1. Is the amount collected for excess wear and tear subject to tax?
2. Is the amount collected for excess mileage subject to tax?
3. Is the disposal fee subject to tax?
4. Is late charge subject to tax?

We would appreciate a letter ruling on the above so that we can ensure compliance with your sales/use tax regulations.

If you have any questions, please do not hesitate to write or call me.

We cannot make a specific ruling regarding these transactions. Please note that the State of Illinois taxes leases differently for Retailers' Occupation Tax and Use Tax purposes than the majority of other states. For Illinois sales tax purposes, there are two types of leasing situations: conditional sales and true leases.

A conditional sale is usually characterized by a nominal or one dollar purchase option at the close of the lease term. Stated otherwise, if lessors are guaranteed at the time of the lease that the leased property will be sold, this transaction is considered to be a conditional sale at the outset of the transaction, thus making all receipts subject to Retailers' Occupation Tax.

A true lease generally has no buy out provision at the close of the lease. If a buy out provision does exist, it must be a fair market value buy out option in order to maintain the character of the true lease. Lessors of tangible personal property under true leases in Illinois are deemed end users of the property to be leased. See the enclosed copy of 86 Ill. Adm. Code 130.220. As end users of tangible personal property located in Illinois, lessors owe Use Tax on their cost price of such property. The State of Illinois imposes no tax on rental receipts. Consequently, lessees incur no tax liability.

The above guidelines are applicable to all true leases of tangible personal property in Illinois except for automobiles leased under terms of one year or less, which are subject to the Automobile Renting Occupation and Use Tax found at 35 ILCS 155/1 et seq.

As stated above, in the case of a true lease, the lessors of the property being used in Illinois would be the parties with Use Tax obligations. The lessors would either pay their suppliers, if their suppliers were registered to collect Use Tax, or would self-assess and remit the tax to the Department. If the lessors already paid taxes in another state with respect to the acquisition of the tangible personal property, they would be exempt from Use Tax to the extent of the amount of such tax properly due and paid in such other state. See 86 Ill. Adm. Code 150.310(a)(3) enclosed.

Under Illinois law, lessors may not "pass through" their tax obligation on to the lessees as taxes. However, lessors and lessees may make private contractual arrangements for a reimbursement of the tax to be paid by the lessees. If lessors and lessees have made private agreements where lessees agree to reimburse lessors for the amount of the tax paid, then lessees are obligated to fulfill the terms of the private contractual agreements.

If the contracts involved were a true lease, charges such as late charges, vehicle disposal fees, excess wear and tear fees and excessive mileage fees imposed at the end of the lease are not subject to tax. However, this answer changes if a conditional sale is involved. For a conditional sale, such fees are costs of doing business that are taxable and should be included in gross receipts. The contract you faxed to the Department appears to be a conditional sale since the title of the vehicle is transferred to your customer. At the time of this initial sale, all gross receipts would be due up front. The fees, however, would not be subject to tax during this transaction because they are only imposed later, when the vehicle is sold back to you at the end of the lease. This later transaction would be an occasional sale if the seller (your original customer) were not otherwise engaged in the business of selling like kind property. This transaction would not appear to be subject to tax. Consequently, the fees you list would be nontaxable as well.

I hope this information is helpful. The Department of Revenue maintains a website, which can be accessed at www.revenue.state.il.us. If you have further questions related to the Illinois sales tax laws, please contact the Department's Taxpayer Information Division at (217) 782-3336.

If you are not under audit and you wish to obtain a binding Private Letter Ruling regarding your factual situation, please submit all of the information set out in items 1 through 8 of Section 1200.110(b).

Very truly yours,

Melanie A. Jarvis
Associate Counsel

MAJ:msk
Enc.